

Expolanka Holdings PLC [EXPO.SL: LKR 45.60]

Strategic relationships and elevated yields to fuel EXPO's growth trajectory

Recommendation: BUY

Target Price: LKR 58.50

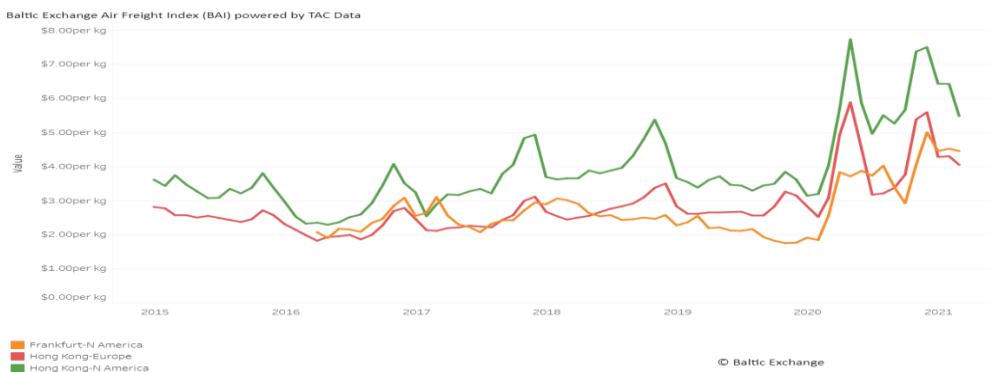
Sector: Transportation

Expolanka Holdings (EXPO)- is ranked 26th largest air freight operator and the 44th largest ocean freight operator in the world, functions predominantly in retail and apparel sectors in USA, contributing to 65-70% of logistics revenue, through EFL (logistics sector contributes to >95% of EXPO's top line in FY21). The group is now controlled by SG Holdings Global Pte. Ltd. the Group's Japan-based parent-who operates in delivery, logistics and real estate sectors with much emphasis on delivery business which involves in express package delivery services and mail express services. EXPO's Asia- North America trade lane is the biggest contributor to EXO's logistics sector with major part of clients being in the US branded apparel sector.

EXPO saw an exponential profit of LKR14.8Bn for FY 20/21 compared to a loss of LKR 737Mn reported a year earlier, mainly helped by higher yields available on the back of low airfreight capacity. EXPO was involved in the shipment of PPE manufactured in Asia to America, and given the urgency managed to secure higher yields which helped to offset the lost volumes. EXPO ended the 2Q'21 with a staggering LKR 4.5Bn profit (cf. loss of LKR 830Mn in 2Q'20), and managed to continue these high level of profits thereafter despite gradual slowdown in PPE shipments, helped mainly by higher yields specially from air freight, and gradual recovery in the usual business volumes (EXPO's profits for 3Q'21 stood at LKR 4.5Bn in cf. LKR 302Mn 3Q'20 and LKR 4.0Bn in 4Q'21 cf. loss of LKR 361Mn in 4Q'20)

Air freight yields expected to remain at elevated levels to help continue with EXPO's margins: Air freight yields that jumped over 2x-3x with unprecedented demand for PPE in 1Q'21, though cooled off with demand easing off, may not see returning to historical low levels in near term given the ongoing constraints in the belly cargo capacity in our view. Although the world CTK (cargo tonne-kilometres) showed a remarkable improvement in the recent past on the backdrop of economic revival, the lack of cargo capacity remains a key obstacle for faster recovery in air cargo business with global ACTK (available cargo tonne-kilometres) still around 12% YoY lower even in March'21. Given that freight charges could only normalize with long-haul passenger flights recovering post vaccination of other countries, we believe the higher than historic level air freight charges to prevail for some time. This should invariably help EXPO given that airfreight contributes to over 70% of logistics income-the biggest contributor of EXPO's topline (>95%).

Global air freight charges could stay at elevated levels in the near term



Key Statistics

Market Cap (LKR Bn)	89.14
Market Cap (USD Mn)	451.4
Issued Quantity (Mn)	1954.9
Current Trading Range	45.20-46.00
52 week High/Low	61.90/1.80
YTD High/Low	61.90/30.90
Valuation	
Market PE (x)	14.5
Market PBV (x)	1.1
EXPO PE (x)	6.0
EXPO PBV (x)	3.3
Bloomberg Ticker	EXPO SL EQUITY
GICS Industry Group	Transportation
Intrinsic Value	58.5
Rating	BUY

Main shareholders as at 31.03.2021

SG Holdings Global Pte. Ltd	75.62
Mr. H. Yusoof	7.52
Mr. F. Kassim	1.20
Nuwara Eliya Property Developers (Pvt) Ltd	0.38
Mr. S. Senthilnathan	0.33

Share Price Performance



Anlyst

: Anjula Nawarathna

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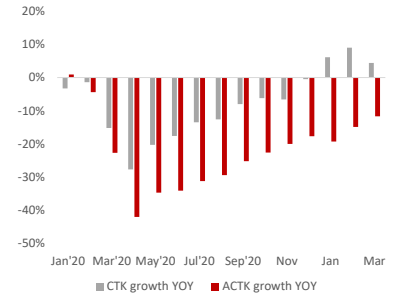
Robust economic activities, particularly in apparel sector in US and subsequent pick-up in volumes to help drive EXPO's topline: The rollout of COVID-19 vaccines and new rounds of government stimulus has lifted consumer confidence for discretionary spending in USA in the recent past. The consumer demand in USA has grown by 10.7% in 1Q'21, after 2.3% growth in 4Q'20, driven by a rapidly improving public health situation and massive government aid to households and businesses that was affected by COVID-19. On this backdrop many companies have raised its expectations for annual profit and sales. For instance, Under Armour Inc- an American sports equipment company that manufactures footwear, sports and casual apparel- has raised its expectation of profits after reporting a 35% jump in revenue as the reopening of economies in the United States.

The J.P.Morgan Global Manufacturing PM – a composite index produced by J.P.Morgan and IHS Markit in association with ISM and IFPSM – meanwhile also has risen to 55.0 in March, a 121-month high and its best reading since February 2011, supported mainly by stronger growth of output, new orders and employment.

We believe all these to have a positive impact on EXPO specially given that EXPO's biggest contribution to the topline is stemming from strong Asia- North America trade lane and that too from the US branded apparel sector. Given that EXPO has managed to more than double its logistics revenue since its restructure in 2016, the expected developments in the global market should bode well with improved volumes thus negating any losses arising from freight yields. Moreover, recent acquisition like Seville Container Freight Station, Inc., Seville Freight Systems Inc., and Seville Transfer Lt- a Bonded Container Freight Station and a Bonded Trucking company located in strategic location like John F. Kennedy Airport should allow EXPO to provide a wider range of value addition services (like freight to be consolidated or deconsolidated in a duty free environment and deliver cargo in a bonded environment) in addition to the primary business, freight services, which should help EXPO to lock in existing clients and have more stronger relationships.

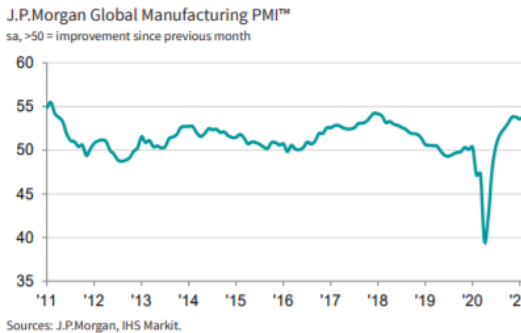
Moreover, EXPO's diversified customer base like continued venture to tech and pharmaceutical tie ups and the strong relationships maintained with both air and ocean freight carriers should also help well with the expected pick up in volumes in our view.

Available cargo capacity is still way behind the demand

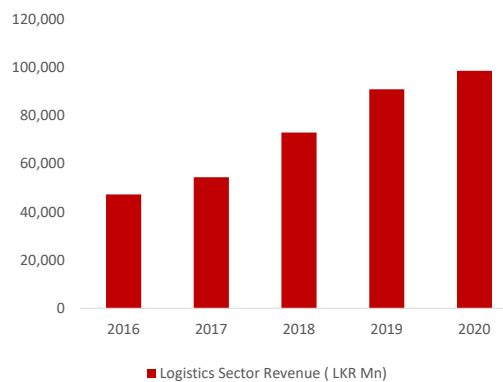


Source : IATA

Global Manufacturing index expands as global economy picks up and services revive



EXPO's logistics revenue more than doubled since restructuring



Source: JP Margon & Company Annual Reports

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Weaker LKR to help EXPO further: Given that majority of EFL's revenue is sourced outside Sri Lanka (contribution from Sri Lanka is just 9% in FY20), we believe any weakness in the LKR could get reflected positively on EXPO's performance. We have conservatively assumed a LKR depreciation of 6%-8% for FY21, thus any decline in global yields too could get set off by weaker LKR in our view.

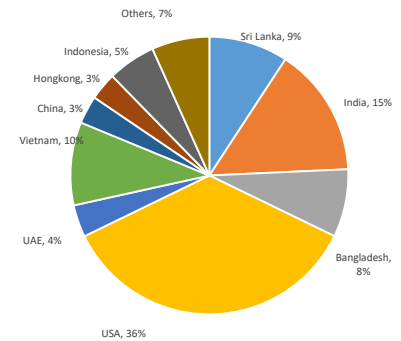
EXPO trades at a hefty discount compared to its global peers, despite ranked 26th largest air freight company in the world. We estimate EXPO's profits to slip to LKR 9.5Bn in FY 2021/22 amid gradual decline in air and sea freight yields, however EXPO could maintain a bottom line of LKR 9-10Bn given the strong rebound in volumes that would come about due to robust pickup in economic activities. EXPO could also look at strategic acquisitions like it did in recent past, to further include more value-added services while also diversifying its customer base by venturing in to new sectors other than apparel.

Despite all these positives however, EXPO still trades at a hefty discount compared to its global peers despite been ranked the 26th largest air freight organization in the world. EXPO currently trades at trailing PE of 6.0x, almost 4 times lower than the average PE of 23x of major listed global logistics giants. Therefore, we firmly believe that EXPO's valuations are currently unwarranted and should be rerated least to 12x on one year forward earnings. Thus, we value EXPO at LKR 58.50 on FY21/22E earnings, a 28.4% higher than the current market prices. If Expo continues with its generous dividend payout of 30%, EXPO should also generate an additional yield of ~3%, bringing up the total return to 31.6%. Thus, we maintain our recommendation BUY.

Earnings Forecast

YE 31 Mar/ (LKR Mn)	FY17	FY18	FY19	FY20	FY21	FY22E	FY23E
Net Profit (Recurrent)	955	711	1,448	1,322	14,828	9,538	9,758
YoY Growth (%)	-14.3%	-25.5%	103.7%	-8.7%	1021.6%	-35.7%	2.3%
Recurrent EPS (LKR)	0.49	0.36	0.74	0.68	7.58	4.88	5.0
Dividend Payout	30.7%	41.3%	20.3%	-15.9%	30.3%	30.0%	30.0%
DPS (LKR.)	0.15	0.15	0.15	0.06	2.30	1.46	1.50
Dividend Yield (%)	0.3%	0.3%	0.3%	0.1%	5.0%	3.2%	3.3%
Price to Sales	1.40	1.15	0.93	0.86	0.41	0.44	0.44
Operating Margin	3.1%	2.4%	3.4%	0.6%	7.7%	7.5%	7.7%
ROE (%)	9.3%	7.0%	12.8%	5.5%	74.0%	31.1%	26.1%
PER - Recurrent (X)	93.4	125.4	61.6	67.4	6.0	9.3	9.1
PBV (X)	6.7	6.4	5.6	6.9	3.3	2.6	2.2

Majority of the logistics revenue is stemming outside Sri Lanka.



Source: Company Annual Report

Average PE of top listed air freight operators are ~ 4x higher than EXPO

Entity	Country of Origin	Current PE
Kuehne + Nagel	Switzerland	34.9
DSV	Denmark	51.5
Sinotrans	China	11.0
UPS	United States	36.4
Expeditors	United States	22.5
Nippon Express	Japan	13.8
Bollere Logistics	France	29.3
Kintetsu World Express	Japan	15.6
Hitachi Transport System	Japan	14.2
Sinotrans Ltd.	China	11.0
Kerry Logistics Network	Hong Kong	14.4
Agility Logistics	Kuwait	51.6
FedEx Logistics	USA	27.1
Dimerco Express Group	Taiwan	11.0
C.H. Robinson Worldwide	USA	22.4
Expolanka (EFL)	Sri Lanka	6.0

Source: Investing.com

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